

**I.T. RULES AMENDED TO ENFORCE PROMPT
PAYMENT FOR SUPPLIES TAKEN FROM
MICRO / SMALL ENTERPRISES (MSEs)**

The Ministry of Finance (CBDT), Government of India has since amended the Income-tax Rules 1962, the salutary effect of which is that –

- (a) delayed payments to MSEs will not only entail payment of interest to the affected MSEs at 18% p.a. **compounded monthly** (effective rate 19.56%)

but will also

- (b) **entail liability to pay income-tax** (at as much as 33.99% presently) on such interest, which is inadmissible as expenditure deductible from taxable income

THEREFORE IT IS WISER

to pay the amounts owed to Micro / Small Enterprises on time and avoid liability to pay INTEREST and INCOME TAX on belated payments.

2. Nature of the amendment

2.1. Reproduced hereunder is the relevant Notification No. 36/2009/F.No.149/86/2008 – TPL published as S.O. 961(E) dated 13th April, 2009 in the Gazette of India, Extraordinary Part II – Section 3 – Subsection (ii):-

**MINISTRY OF FINANCE
(Department of Revenue)
(CENTRAL BOARD OF DIRECT TAXES)
NOTIFICATION
New Delhi, the 13th April, 2009
INCOME-TAX**

S.O. 961(E). – In exercise of the powers conferred by Section 295 read with Section 44AB of the Income Tax Act, 1961 (43 of 1961), the Central Board of Direct Taxes hereby makes the following rules further to amend the Income-Tax Rules, 1962, namely:-

1. (1) These rules may be called the Income-tax (10th Amendments) Rules, 2009.
- (2) They shall come into force on the date of their publication in the Official Gazette.

2. In the Income-tax Rules, 1962, in Appendix II, in Form No. 3CD, after item 17, the following shall be inserted, namely:-

“17A. Amount of interest inadmissible under Section 23 of the Micro, Small and Medium Enterprises Development Act, 2006”

[Notification No.36/2009/F.No.149/86/2008-TPL]

ANAND KUMAR KEDIA, Director (TPL-III)

Note:- The principal rules were published in the Gazette of India, Extraordinary, Part II, Section 3, Sub-section (ii) vide S.O. 969(E), dated the 26th March, 1962 and last amended by No.S.O.866(E), dated 27-3-2009.

2.2. The amended I.T. Rule re-inforces compliance (*by all “buyers” of goods and services from Micro / Small Enterprises*) with Sec. 23 of the “Micro, Small and Medium Enterprises Development Act, 2006” (Act 27 of 2006) which provides as follows:-

“23. Interest not to be allowed as deduction from income

Notwithstanding anything contained in the Income-tax Act, 1961 (43 of 1961), the amount of interest payable or paid by any buyer, under or in accordance with the provisions of this Act, shall not, for the purposes of computation of income under the Income-tax Act, 1961 (43 of 1961), be allowed as deduction.”

2.3. It will kindly be appreciated that this amendment has to be read with the provisions in Chapter V of the MSMED Act.

3. Implications of the amendment

3.1. In simple terms, this means that if any ‘buyer’ of goods / services from Micro / Small Enterprises (MSEs) defaults in paying for the supplies promptly, as provided for in Chapter V of the MSMED Act -

- (a) the defaulter has **perforce to pay interest for the period of delay at 3 times the bank rate of interest notified, from time to time, by RBI** (which is presently 6% and three times thereof will be 18% p.a.) **COMPOUNDED WITH MONTHLY RESTS, notwithstanding any condition to the contrary in the contract between the ‘buyer’ and the ‘supplier’ MSE.**

AND

- (b) **perforce bear liability to income-tax thereon, as such interest on delayed payments to MSEs (*whether already paid or remaining accrued due and payable*) will be added to the taxable income of the ‘buyer’ and subjected to income-tax, year after year, until it is finally paid to the affected MSEs.**

3.2. It is important to note that the stipulation for payment of interest, COMPOUNDED WITH MONTHLY RESTS has a cumulative effect, keeping alive, year after year, not only the liability to pay interest until finally paid off to the affected MSEs in full settlement, but also the liability to pay the income-tax thereon every year. **THEREFORE, THE ONLY WAY FOR THE ‘BUYERS’ TO GUARD AGAINST SUCH INTEREST AND INCOME-TAX LIABILITY IS TO PAY PROMPTLY THE SUPPLY BILLS OF MSEs.**

3.3. The amendment inserts new item 17A in Form 3CD prescribed under the IT Rules. Form 3CD is the ‘**TAX AUDIT REPORT**’ to be filed by the Statutory Auditors of Assesseees for whom such audit is made mandatory u/s. 44AB of the IT Act (if their annual sales turnover is Rs.40 lakhs and above)

3.4. Thus, the underlying significance of this amendment is that, a **DUTY IS NOW CAST ALSO ON THE AUDITORS OF THE (BUYERS) ASSESSEES -**

- (a) to ensure that the statutory interest is computed on any belated payments of MSEs’ Bills; and the same is
- (b) reported in Form 3CD relating to the assessee; and further ensure that it
- (c) is also disclosed in the I.T. Returns, in the relevant column therein (to get added to the taxable income); and
- (d) the appropriate income-tax is paid thereon, before filing the I.T. Return.

3.5. Consequently, the underlying merit of the present amendment is that -

- (a) what has hitherto been only the responsibility of the ‘buyers’ from MSEs who default in complying with the provisions of Chapter V of the MSMED Act (relating to prompt payment of MSEs’) Bills to abide by the deterrent provisions therein, like disclosure in their Balance Sheets and I.T. Returns and payment of income-tax,
- (b) **has now been made the responsibility of the buyers’ auditors also, to ensure compliance thereof**

And thus, the last missing link in the scheme of ensuring compliance has been provided by this I.T. amendment.

3.6. It is pertinent to add that the officers of the Directorates of Industries in the various State Governments (designated u/s. 26 of the MSMED Act to monitor compliance with the provisions of the Act) are also vested with powers to -

- (a) call for information from any 'buyer' regarding compliance with the stipulations in Chapter V of the Act, in the matter of (i) period of credit (maximum 45 days) imposed on MSEs; (ii) payment of the mandatory interest for delayed settlement of MSEs' Bills; and in case of defaults (iii) disclosure of overdue principal and interest in the annual Balance Sheets and (iv) disclosure of interest on delayed payments in the Annual I.T. Returns and (v) payment of appropriate income-tax thereon; and
- (b) in the event of failure to furnish the information called for, to impose a fine of not less than Rs.10,000/-

Thus, apart from the Statutory Auditors, the designated officers u/s.26 of the MSMED Act have also been made responsible to ensure compliance.

4. In the circumstances, all the Industry Associations / Chambers of Commerce, the Institute of Chartered Accountants of India, the Institute of Company Secretaries of India etc should publicise amongst its members, the imperative need for all Large, Medium (and even Small Scale) units who source materials / services from MSEs to effect prompt settlement of the latter's Bills and save themselves from the rigours of the penal provisions in the Act, **which automatically come into operation, without involving the affected MSEs.**